



**BAKER TILLY**

Third Floor  
One London Square, Cross Lanes  
Guildford, GU1 1UN  
United Kingdom

T: +44 (0)844 2640300

[www.bakertilly.co.uk](http://www.bakertilly.co.uk)

Mr Gary Pflugrath  
Project Director  
International Auditing and Assurance Standards Board  
545 Fifth Avenue, 14<sup>th</sup> Floor  
New York  
New York 10017  
USA

[hugh.morgan@bakertilly.co.uk](mailto:hugh.morgan@bakertilly.co.uk)  
15 May 2013

Dear Mr Pflugrath

**Consultation Paper: “A Framework for Audit Quality”**

Thank you for the opportunity to comment on the IAASB’s consultation paper on audit quality.

Our responses to the specific questions raised by the IAASB in their Invitation to Comment are included in the Appendix. Our main comments are summarised below:

1. Overall support – we are supportive of the IAASB’s Audit Quality Framework but in our opinion the Framework is too long and we believe that SME auditors, particularly those in countries with less developed corporate reporting and auditing regimes, who would perhaps most benefit from such a Framework, would find it difficult to put into practice.
2. Update ISQC 1 and ISA 220 – whilst the Framework raises important issues, in our view it would be better for the IAASB to concentrate their resources on updating the existing authoritative requirements and guidance in ISQC1 and ISA 220 rather than potentially confusing auditors and creating regulatory issues with additional, what looks like authoritative, guidance on audit quality.
3. Think small first – in our view the Framework should be tailored to meet the needs of those firms performing SME audits and make it easier for those firms to operationalise the Framework and put it into practice.
4. IFAC to publish - to avoid confusion with the existing authoritative standards on audit quality we believe that it would be more effective if the Framework was issued by IFAC rather than the IAASB. This would help to make it clear that the Framework did not have the same status as the audit quality requirements for auditors in ISQC1 and ISA 220 and place it more appropriately within the wider more practice oriented guidance of IFAC.



Please contact me should you wish to discuss any of the points raised in this response.

Yours sincerely

A handwritten signature in blue ink, appearing to read "H Morgan".

Hugh Morgan  
Technical Director  
Baker Tilly UK Audit LLP



## Appendix

### Response to specific questions asked by the IAASB

**Q1: Does the Framework cover all of the areas of audit quality that you would expect? If not, what else should be included?**

YES

In our view, the Framework appears to cover all of the areas of audit quality that we would expect it to. We are supportive of the way that the Framework has been structured around input factors, output factors, key interactions and contextual factors. Our reservations about the Framework are not that something is missing but rather that the Framework is too long to be a practical solution for auditors seeking to improve audit quality, particularly those auditors in the SME sector who might most benefit from such a Framework. We also question how the Framework is intended to be used because it is difficult to understand how it could be put into practice.

As a result, we would not support additional material being added to the Framework because that would make the Framework even longer and even less likely to be used by auditors. We recommend that the IAASB focuses on cutting the Framework down to a more manageable size, tailoring it to the needs of auditors of SME companies and make it easier for those audit firms to operationalise.

**Q2: Does the Framework reflect the appropriate balance in the responsibility for audit quality between the auditor (engagement team and firm), the entity (management and those charged with governance), and other stakeholders? If not, which areas of the Framework should be revised and how?**

NO

In our opinion, the Framework does not reflect the appropriate balance in the responsibility for audit quality between the auditor (engagement team and firm), the entity (management and those charged with governance), and other stakeholders.

We are supportive of the way the IAASB has tried to involve a wide range of interested parties but we consider that the consultation paper over-emphasises the importance of management and those charged with governance in achieving the audit quality aims. The role of management and those charged with governance is important but in our opinion, whilst we agree that management and those charged with governance have an indirect positive impact on audit quality they may also have a negative impact on audit quality which is not touched on by the consultation paper at all. The Framework could place greater emphasis on the importance of interactions with standard setters and regulators and their impact on audit quality.

**Q3: How do you intend to use the Framework? Are there changes that need to be made to the form or content of the Framework to maximise its value to you?**



We will follow closely the development of the Framework but do not expect it to have much impact on UK auditing. The UK is a sophisticated audit and corporate reporting environment which has developed over the years and thanks to the work of the FRC we are leading the way on a number of areas including audit quality. Although we question how useful the Framework will be in a UK auditing environment we can appreciate that in countries where the audit and corporate reporting environment is less sophisticated and auditors are having to step up to meet the increased demands of international auditing and accounting standards that the Framework could help those countries put in place the necessary audit quality foundations that would allow them to develop in the international market.

As stated above in our response to question one, we believe that the current Framework is too long and is structured in such a way that SME auditors in particular would find it very difficult to put into practice. We are also concerned about what status the audit quality Framework will have and the way in which the Framework will interact with existing IAASB audit quality requirements for auditors at a firm level in ISQC 1 and at an individual audit level in ISA 220.

There is a real danger that if the Framework is used in its current form it will not only distract auditors from complying with ISQC 1 and ISA 220 but also, if it is not used, that auditors will be measured by their regulators against the audit quality standards set out in the Framework. In our opinion, the IAASB should make it clear how they expect the Framework to be used by different stakeholders and the relative status it will have against the requirements in other IAASB authoritative material on audit quality in ISQC 1 and ISA 220. In our view, it would help to distinguish the status of the Framework from the more authoritative IAASB material if the Framework was issued by IFAC instead of the IAASB.

As stated above, in our opinion we believe that the IAASB should concentrate its limited resources on updating and improving the existing quality standards ISQC 1 and ISA 220 rather than issuing potentially conflicting and confusing guidance in a separate document that has no authoritative status. If the IAASB were updating ISQC 1 and ISA 220 there are a number of points in the Framework that could usefully be added to ISQC 1 or ISA 220 in the form of explanatory guidance but we would caution against including any new requirements.

**Q4: What are your views on the suggested Areas to Explore? Which, if any, should be given priority and by whom? Are there additional Areas to Explore?**

Our views on each of the suggested Areas to Explore are given below:

***1. Establishing global guidance against which audit firms can assess their governance arrangements.***

We support the IAASB's aim of establishing global guidance against which audit firms can assess their governance arrangements. The UK has for many years had a successful corporate governance code that operates for listed companies and has helped to establish good corporate governance practices within UK listed company boards and audit committees and has improved the transparency with which boards and audit committees communicate with shareholders. However,



the UK corporate governance code is restricted to listed companies and not to companies that are not listed even though they may be quite large.

If global corporate governance was developed for audit firms we would be concerned whether it would be practical in all jurisdictions and in particular whether it would be relevant to auditors of SMEs. There are matters that are common to all firms, no matter what size, such as professionalism, compliance and risk management, but in our opinion these matters might be better dealt with through improvements to the existing guidance in ISQC1 and ISA 220 rather than the addition of a new piece of guidance.

**2. *Establishing a common understanding of capabilities, and how they are demonstrated and assessed, as they relate to audit quality for use by audit firms when recruiting, evaluating, promoting, and remunerating partners and staff***

This is a very important area to explore and one which applies to all auditors including those of SMEs. Making sure that audit teams have the appropriate capabilities to carry out audits is of critical importance to ensuring that high quality audits are performed. The professional accountancy bodies responsible for qualifications should ensure that this aspect is emphasised at the start of training for the qualification and that professional development, ethics and professional scepticism are viewed as key components of the qualification.

We believe that many parties, including standard setters, education providers, regulators and professional bodies have key roles to play in helping to ensure that auditors do have the appropriate capabilities that will enable them to perform high quality audits and that audit firms should prioritise achieving high audit quality as their main objective.

**3. *Improving information sharing between audit firms when one firm decides to resign from, or is not reappointed to, an audit engagement.***

Whilst sharing information between audit firms on changes of appointment is an important issue, in our opinion it is more of a process matter rather than one to be prioritised as an audit quality matter by the IAASB. This process is already well regulated in the UK and across Europe as a result of the implementation of the European Union's Statutory Audit Directive. Article 23(3) of this Directive states that: "where a statutory auditor or audit firm is replaced by another statutory auditor or audit firm, the former statutory auditor or audit firm shall provide the incoming statutory auditor or audit firm with access to all relevant information concerning the audited entity". Nevertheless, practice does vary internationally and we believe it would be helpful for the IAASB to encourage countries to introduce national law and regulation that provides for the necessary information flow between auditors.

**4. *Considering whether audit inspection activities can do more to improve audit quality and to make audit quality more transparent to users.***

In our view, the process of audit inspection plays an important role in improving audit quality through the inspections themselves and the reports provided to firms



and regulators. In the UK, audit inspection activities have helped make audit quality more transparent to users through public reports issued on the larger firms by the FRC and more general public reports issued by other inspection bodies such as the ICAEW. It is important that these public reports are balanced and emphasise the good points as well as the more negative ones. Too much emphasis on the negative points only serves to undermine audit quality rather than improving it. Although regulators are important, this should not be over-emphasised and it is important to remember who the users of the financial statements and what the true and fair view encompasses.

- 5. Exploring whether there would be value in national authorities responsible for determining sanctions on auditors exchanging information with a view to evaluating the relative effectiveness of their different arrangements.***

In our view there would be some value in national authorities responsible for determining sanctions on auditors exchanging information with a view to evaluating the relative effectiveness of their different arrangements. However, we do not consider that this should be a priority project for the IAASB and that other areas to explore are more worthy of exploration.

- 6. Considering “root causes” and best practices by regulators, audit firms, and the wider audit profession in order to learn from past audit deficiencies and to identify and address systemic issues.***

We agree that it is important to examine “root causes” to determine whether there are any underlying reasons for audit quality failures. In recent years the auditing profession has responded to several high profile audit failures and the pressure of the recession by becoming even more inward looking with firms continuously reviewing their strategies, policies and procedures and the level of inspection performed both internally by the firms and externally by the independent inspection bodies has increased enormously combined with greater transparency from the public reports on the larger firms. Whilst auditors and firms can always improve it is difficult to see how much an IAASB project in this area can add to what is already being done.

- 7. Increasing the informational value of auditor’s reports and improving perceptions of the value of audit.***

The content and informational value of auditor’s reports is an important area both internationally and in the UK and the IAASB and FRC both have on-going projects in this area. We are in full support of the priority that the IAASB has given to the audit reports project and, in our opinion, the IAASB is making good progress in trying to produce and internationally consistent auditor’s reports. We have encouraged the FRC in the UK not to diverge from consistency with IAASB standards and have urged them to work with the IAASB to develop an internationally consistent auditor reporting model.

We are still unconvinced about how the perceptions of the value of audit can be improved through the auditor’s report and have cautioned the IAASB about the dangers of original reporting by auditors because we strongly believe that it is the



directors responsibility as preparers of the financial statements to make full disclosure and not for the auditors to fill the gaps.

**8. *Achieving improved two-way communication between auditors and financial and prudential regulators, particularly in the financial services sector.***

We agree that the IAASB should be seeking to achieve improved two-way communication between auditors and financial and prudential regulators, particularly in the financial services sector. We have supported the efforts made by the IAASB to improve two-way communication between auditors and those charged with governance in ISA 260 and this has been well received in the UK where we had promoted two-way communication between auditors and audit committees for a number of years. We support two-way communication being extended to financial and prudential regulators and would encourage international adoption of good practice on this type of two-way communication. This should enhance both the effectiveness of audits and the auditor's contribution to prudential regulation.

**9. *Striving for greater international harmonization in the role of audit committees with regard to the evaluation of the quality of the external audit.***

We agree that there should be greater international harmonization in the role of audit committees with regard to the evaluation of the quality of the external audit. The UK is already far advanced with this process with the UK Corporate Governance Code for listed companies and the requirement for aspects of this to be reported on by auditors.

The evaluation of the quality of the external auditors is one of the main tasks of the audit committee and although this does not apply to auditors of SMEs we do consider that the IAASB should develop guidance and seek greater international harmonization.

**10. *Encouraging audit committees to provide more information to users of the financial statements on the work they have undertaken, the main issues they have addressed, and the reasons for their conclusions.***

This is an important aim and we support the IAASB in encouraging greater transparency regarding the work of audit committees. The FRC in the UK has made important strides in this area in its corporate governance requirements and code and the recent changes made to auditors' reports.

In our opinion, auditors should not be responsible for original reporting about the client on financial reporting matters. The requirements of IFRS are very clear and require that the financial statements make specific disclosures including areas where there are critical accounting estimates and judgements. It is important that the IAASB work with its colleagues the IASB to ensure that the financial reporting requirements are followed by the directors and that auditors are not called on to fill the gaps simply because they are required to follow standards. Audit committees are an important part of this and in the UK they are now required to disclose the significant matters that the auditors discussed with them.